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THE ITALIAN NEW RESIDENT TAX REGIME

An attractive tax rule for wealthy individuals transferring their tax residence to Italy

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The Italian Budget Law of 2017 introduced a new special tax regime for Individuals who transfer their tax residence to Italy from January 1st, 2017. This special tax regime is particularly attractive to high net worth individuals and families, because it grants a reduction of the tax base to the domestic income and gains only and, in comparison with other special regimes (e.g. the Swiss globalist or the UK res-non-dom) it offers a high degree of privacy to the taxpayer.
The special regime is applicable to both Italian and foreign citizens. The Law also provides a preferential route (”golden visa”) for non-EU citizens.
The new law sets a “substitute tax regime” on foreign-sourced income and gains, including effects related to inheritance and gift taxation, as described below in greater detail.
We have many cases currently in progress, one of which has already successfully concluded, and we can confirm from our experience that this new tax regime works and is suitable for any person who matches the criteria that we are going to explain hereinafter.

The “Italian New Resident” conditions

The substitute tax regime is available on option to Individuals, whether Italian or foreign citizens, who acquire Italian tax residence, subject to the following conditions:
(i) The individual must have been non-resident of Italy, pursuant to Italian income tax law, in at least 9 of the 10 years prior to the first year of effect of the option for the substitute tax regime; and
(ii) The individual obtains a ruling from the Italian Tax Authorities, according to general laws;
(iii) The option is available for 15 years only.

(i) The “9 out of 10” rule
For income tax purposes, as ruled by Art. 2(2) of the Consolidated Italian Tax Code, an individual is deemed to be a resident of Italy if at least one of the following conditions is fulfilled for most part of the year (the tax period coincides with the calendar year and there is no split-year concept):

a) He/she is registered with the Italian Official Register of the resident population ("anagrafe della popolazione residente"). Registration in the Italian Official Register of the resident population is a formal condition, which is by itself sufficient in order to be deemed tax resident; or
b1) He/she has his/her residence in Italy for civil law purposes. According to Italian rules it should be considered the habitual abode, which is determined by two factors: (1) the objective circumstance of the individual being in Italy, and (2) the intention to steadily (i.e. not temporarily) remain there; or
b2) He/she has his/her domicile in Italy for civil law purposes. Domicile is defined by the Civil Code as the place in which a person establishes the main seat of his/her business and interests. Both economic and family/social ties have to be taken into account.

The Italian notion of residence and of domicile is completely different from the English notion. Similarly to France, Italian Judges generally regard the centre of vital interests, i.e. the place where personal and economic relations are closer and/or the effective place of the habitual abode.
Generally, in order to be regarded as non-resident in Italy the taxpayer must be enrolled in the Register of Citizens living Abroad ("AIRE Anagrafe Italiani Residenti all'Estero"). Although this condition is necessary, it is not regarded as sufficient. A specific analysis of the Italian residence and domicile should be made, considering the above said rules. In particular the "183 days" rule must be considered.
For many jurisdictions (e.g. Switzerland), as described by § 2 of Art. 2 of the Italian Consolidated Tax Code, the law sets an inversion of the burden of proof upon the taxpayer. A rebuttable presumption is set by law stating that a citizen resident abroad within a black list jurisdiction is deemed to be Italian tax resident if not proved to the contrary. The above mentioned issues are very well known by the Italian praxis and we have the support of cases passed by Italian courts. The tax residence assessment should be an important preliminary activity to be performed, for both black list or white list countries of tax residence.
Having said that, we believe that the approach of the Italian Authorities on this rule will be very substantial and less formal, enquiring where the candidate has been truly and genuinely resident abroad.
Clearly, the applicable international treaties should be considered.

(ii) The ruling from the Italian Tax Authorities
The candidate must sign his/her option within the standard deadline for tax returns related to the specific tax year, which in Italy for Individuals follows the calendar year. Generally the deadline is therefore on September 30th of the subsequent tax year.
According to the law, the scope of the ruling should be limited to the confirmation that the individual has been non-resident in Italy in at least 9 of the 10 years prior to the first year of effect of the option, so that the ruling request may be filed prior to the transfer of residence to Italy.
A specific procedure is set. Italian Tax Authorities must reply to the ruling request within 120 days; Additional information and documentation could be requested, but only on one occasion. Following this communication, a new deadline of 60 days starts to run from the reply to such request of additional information and documentation. Lacking a reply within the above deadline, a positive reply is deemed to have been rendered, welcoming the candidate to the new regime.
According to the law, the taxpayer can request the exclusion of one or more foreign states from the application of the new regime. The effect is therefore that the income and gains deriving from such excluded countries are included in the domestic taxable base of the taxpayer. A procedure is in place to inform both the Italian Tax Authorities and the Authorities of the other relevant jurisdiction in the year prior to the first year of effect.

Furthermore on May 23rd the Italian Tax Authorities published the official interpretation of this law with Circular Newsletter n. 17/E/2017. The Tax Authorities position is pragmatic and gives a strong reassurance about interpretation of the law.
Following the Tax Authorities interpretation is necessary to take a deep look to income flows in order to find out any eventual interposed entity or company having income in Italy or abroad; it gives room to trust and estate planning following the (new) International praxis, avoiding the risk of recapture of income such as CFC rules. This element is also relevant for governance issues and planning, in particular with regard to holding companies where the new Italian taxpayer is the sole director. In such a case, it is likely that the company governance needs to be re-organized whilst, on the other hand, comfort is granted to new Italian Resident being part of the board of directors on foreign companies with substance over form.
Similar pragmatic approach is also taken for Gift and Inheritance tax legislation. Once the new Italian Resident is within the new regime his or her wealth could be wisely re-organized, following the principles of Italian tax laws, achieving an exemption with regard to assets held abroad.
Last but not least, the Tax Authorities clarified that there is no need for full disclosure of assets existing outside the Italian territory, although we still believe that a pragmatic approach with a ruling is to be preferred, in particular for those applicants coming from black list countries or with a complicate estate planning.
The Circular sets several other information on procedures and "impatriates workers", providing full comfort to the applications (already started). Once again Italian Tax Authorities gives a clear guidance, demonstrating full technical capabilities and a pragmatic approach. Our Firm will continue to monitor the evolution of this important planning tool, to be wisely regarded among the various tools of wealth planning in full compliance with tax and regulatory guidelines worldwide.

(iii) The 15 years rule
The option for the substitute tax regime is effective up to a maximum period of 15 years. And it must be applied every year, failing which the regime is no longer applicable. Basically the rule is aimed to avoid any "cherry picking" planning over the years. There is no penalty for leaving the option, with the sole consequence that the tax regime reverts back to the worldwide principle of taxation.

The "Italian New Resident" regime

The Italian New Resident regime provides for:
(i) A substitute tax on all foreign-sourced income and gains;
(ii) A mandatory exclusion from the scope of the substitute tax for capital gains on substantial shareholdings realized in the first 5 years of effect of the option;
(iii) An optional exclusion for income and gains sourced in selected foreign states;
(iv) Additional benefits for the purposes of reporting obligations, wealth taxes and inheritance and gift tax;
(v) Specific rules applicable to family members.

(i) The substitute tax on foreign-sourced income and gains
The new regime carves out (by option) all foreign-sourced income and gains. In order to be effective, a substitute tax equal to Euro 100,000 per year should be paid. Such tax applies irrespectively of the (effective) amount of foreign-sourced income and gains, which are not disclosed to the Italian Tax Administration.
The law provides that the substitute tax cannot be reduced by any foreign tax credit. The income and gains within the scope of the substitute tax are not subject to any additional income taxation, even if remitted to Italy. The rule defines foreign-sourced income and gains by making reference to the same criteria that are relevant to determine whether an income or gains is regarded as Italian-sourced

income and therefore taxable in Italy upon a non-resident. The relevant principle is therefore of a territorial basis in comparison with the worldwide taxation principle which is generally applicable to Italian residents. Basically, it is the application of the Italian general rule, but with a reduced tax base, excluding foreign-sourced income and gains.

(ii) The mandatory exclusion related to substantial shareholding in the first 5 years

A particular rule is applicable and it could be regarded as a formal anti-abuse one. Capital gains (and losses) on substantial shareholdings realized in the first 5 years of effect of the option are excluded from the scope of the substitute tax and are subject to income tax under general rules with the benefit of a foreign tax credit (subject to general conditions and limitations). Clearly the aim is to avoid a speculative approach related to a short change of tax residence in order to avoid (other jurisdictions) foreign tax rules[1].

(iii) The optional exclusion for income and gains sourced in selected foreign States

According to the new law, within the necessary option the taxpayer could opt out for all income and gains sourced in one or more foreign States. Accurate tax planning assessment shall be taken when deciding for the application of the option of the Italian New Resident regime. Guidance will certainly be given by tax authorities, according to the law.

(iv) Wealth taxes, inheritance tax, gift tax and fiscal monitoring

For taxpayers who opted for the new regime a reduction of the tax burden is applicable in relation to the fiscal monitoring (RW model in the Italian tax return)[2], as well as concerning wealth taxes, stamp duties, IHT or gift taxes related to assets held abroad[3]. Again a system that excludes any foreign assets from the application of the general rule, which is therefore reduced to the territorial basis only. Clearly a good incentive for those taxpayers who are going to make use of the new regime to re-organize their international estate planning in full compliance.

(v) Extension of the new regime to family members

The regime can be extended to one or more qualifying family members, provided they fulfil the 9 out of 10 years non-residence condition, against the payment of an annual substitute tax of 25,000 Euro (rather than 100,000 Euro) per each family member benefitting from the regime. Therefore, if for example, two spouses transfer their tax residence to Italy and both of them wish to benefit from the substitute tax regime, the overall annual substitute tax would be limited to 125,000 Euro. If the individual subject to the 100,000 Euro substitute tax revokes the option, then the substitute tax regime automatically ceases to apply also to the qualifying family members. On the other hand, the extension of the substitute tax regime to qualifying family members could be withdrawn without affecting the application of the substitute tax regime to the individual subject to the 100,000 Euro substitute tax.

Definition of qualifying family members can be found in the general Italian rules (e.g. Art. 433 of the Italian Civil Code) considering the case of somebody bound to pay legal allowances to support a family member. The new rules for same-sex marriage and civil unions will be applicable, according to the law.

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[1] A disposal of a "qualified shareholding" generally arises if the shares sold in the last 12 months (a) represented more than 2% of the voting rights of a company listed on a stock exchange or more than 20% of voting rights of other companies, or (b) more than 5% of the share capital of a company with shares listed on a stock exchange or more than 25% of the share capital of other companies.

[2] Italian Resident individuals are generally subject to reporting obligations on foreign-held assets that are either owned or beneficially owned (e.g. in the capacity of beneficiary of a trust) or in any case at their disposal. The specific rule should be considered also in relation to the concept of ultimate beneficial owner associated to AML legislation. Misreporting is heavily sanctioned.

[3] Including IVIE (the wealth tax for foreign real estate) and IVAFE (the wealth tax for bankable assets held abroad).

We believe that tax authorities will maintain a substantial approach, in order to provide certainty to the regime. As previously mentioned, this is a benefit of the ruling provided by the procedure in place.

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